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CITICORP

July 7, 1997

Mr. John P. Galligan, Director
Card Technology Division
Financial Management Service
U.S. Department of the Treasury
Room 526
Liberty Center
401 14th Street, S.W.
Washington, D.C. 20227

Re: Citicorp's Comments on the Financial Management Service's Proposed Rule, 31 CFR Part 207, regarding Electronic Benefits Transfer, Selection and Designation of Financial Institutions as Financial Agents
-- RIN 1510-AA59

Dear Director Galligan:

This letter is submitted to the Financial Management Service ("FMS") of the U.S. Department of Treasury by Citibank EBT Services in response to the FMS request for comment on the proposed regulations (62 FR 25572) (the "EBT Regulations") codified at 31 CFR Part 207, regarding the selection and designation of financial Institutions as Financial Agents for Direct Federal Electronic Benefits Transfer to implement the Debt Collection Improvement Act of 1996 (the "DCIA"). Citibank EBT Services is the leading provider of EBT services in the country and we support the goal of developing a nationwide integrated EBT system utilizing the commercial infrastructure for the delivery of government benefits. We believe that only through a public-private partnership can an EBT system be created that will provide recipients with a safe, reliable and economical means to access their benefits.

While we are pleased that FMS has laid the groundwork for creating an EBT system for the disbursement of Direct Federal benefits, we are concerned that the proposed rule limits accountability of the financial institution solely to Treasury and does not recognize the relationship between the beneficiary and the financial institution. Our comment addresses this limitation and suggests a different model for the relationship among Treasury, the Financial Agent and Direct Federal benefit recipients.

For the reasons set forth below, we believe that the proposed rule, as written, does not adequately account for the relationship between the recipients' ownership of Direct Federal benefit funds and the duties owed by the Financial Agent. We believe that the rule should 1) recognize that a relationship is created between the Financial Agent and the recipient upon deposit of the funds; 2) establish service guidelines for the accounts provided by Financial Agents to recipients; and 3) state minimum qualifications for a regulated financial institution to become a Financial Agent for the distribution of Direct Federal benefits.

207.033

Proposed Section 207.3 (b) provides that "the financial agent shall act solely as the agent of the United States, not as the agent of the unbanked recipient, and shall only be accountable to the Treasury." We believe that this proposed regulation does not respect the traditional duty of a depository to its depositor and does not appropriately protect the interests of unbanked recipients. We believe that the desired goals of providing account services to unbanked recipients and the appointment of Financial Agents for the Treasury can be accommodated while still permitting the financial institution to be accountable to benefit recipients.

In the traditional world of banking, when a person opens a deposit account with a financial institution, the relationship created is that of depositor and depository. This historical relationship has resulted in the creation of a vast body of law addressing this relationship and well-defined duties that a financial institution has toward its depositors. These duties have provided the basis for most consumer protections, including those afforded by numerous Federal regulations, such as Regulations D, E and CC. The relationship between the depositor and his depository normally arises out of a choice the depositor made in opening an account at the financial institution and placing on deposit funds owned by the depositor. This ownership interest in the funds on deposit is fundamental to the depositor-depository relationship.

The provision of financial services has changed considerably in the last two decades so that paper, either bank notes or checks, are no longer necessary, and are, in fact, somewhat undesirable, to make deposits to an account. The elimination of paper on the deposit side of banking is mirrored on the withdrawal side, so that depositors can also make use of electronic funds transfer (EFT), through debit cards and other electronic methods, to realize the value of deposited funds. The fact that the funds are now digitally represented does not change the depository relationship when the depositor directs his deposits or his withdrawals to be made electronically . A set of rules, both federal and private, have been developed to regularize this movement of funds and to place responsibility as appropriate, with many of these rules designed to protect consumers. Indeed, the whole premise of the Federal Direct Deposit Too program and Direct Federal EBT is to make use of commercial EFT systems, and the public and private rules governing their use, for the distribution of Direct Federal benefits to recipients.

Because EFT has become so commonplace, one of the goals in moving the distribution of government benefits from paper instruments to electronic distribution was to provide to benefit recipients the advantages of the safe, reliable and economical means of accessing their benefits available to accountholders at most financial institutions today. In the distribution of Direct Federal benefits, we do not believe that there should be any difference in the rules governing the treatment of banked recipients and unbanked recipients. Yet with proposed 207.3, there will result a glaring difference: when a banked recipient receives funds in his deposit account, the financial institution will have an obligation to that accountholder; for the unbanked recipient, there will be no such obligation.

The stated premise of the proposed regulation is that there are sufficient distinctions between the usual transfer of funds to benefit recipients through EBT and transfers to account-owning benefit recipients through direct deposit that the usual rules applying to depository relationships justify a different treatment of these two groups. The distinctions offered, however, are insufficient to support such different treatment.

The three distinctions asserted can be restated as: 1) direct deposit is for accountholders who have chosen their account attributes and EBT is for the unbanked who have accounts with attributes chosen for them; 2) Treasury's responsibility for a direct deposit payment ceases once an ACH transfer is originated, but with EBT, since Treasury is also directing the creation of the account, its responsibility continues, and 3) in direct deposit, the contract between the depositor and depository determines his access to the funds, and with EBT, it is the contract between Treasury and the Financial Agent that determines recipient access. While these distinctions may be useful potentially to distinguish EBT accountholders from other accountholders (we say potentially, since the exact terms that Treasury requires may in fact leave no distinction between recipients using existing bank accounts and those

who are as yet unbanked), they are not relevant to the more fundamental issue of ownership of the funds. Ownership of the funds is fundamental to defining relationships and duties in consumer banking.

The language of the proposed regulation, "the financial agent . . . shall only be accountable to the Treasury", suggests that the funds remain under the control of the United States, after the funds are in the account in the name of the recipient. The proposed regulation appears to delay transfer of ownership of the funds from the date of the transfer to the date of access of the funds by the recipient. Thus, a benefit recipient that has direct deposit would have ownership of the funds sooner than an EBT recipient. We do not believe that there is any basis in the relationship between Treasury and the Financial Agent that warrants the continued control over funds after their credit to the account of the recipient.

Contrary to the apparent scheme of the proposed regulation, we believe that the act of initiating the transfer to a deposit account of the benefit recipient has the same effect for those recipients using direct deposit as for those recipients using EBT-- that is payment to a creditor of the United States, which satisfies the obligation of the United States with respect to that creditor and the substitution of the obligation of the depository for the obligation of the United States. Acknowledging this transfer of obligation in the regulation effects one more important change--it provides unbanked recipients with the same status as banked recipients.

The requirement that the financial agent be only accountable to the Treasury also appears to be inconsistent with the requirement that the account be FDIC insured and subject to Regulation E. For both deposit insurance purposes and Regulation E, the duty with respect to the account flows from the financial institution to the accountholder, and not to a person who happens to direct a deposit to the account.

This requirement for accountability only to Treasury is unnecessary for Treasury to accomplish its goal of providing financial services to unbanked recipients of direct federal payments. We believe that the Secretary of the Treasury has the authority to request that Financial Agents perform such other duties as may be required of them from time to time. To give effect to the intent of the DCIA, which allowed the government agencies to explore a variety of means to comply with the DCIA, we believe that the Secretary can set guidelines for deposit accounts provided by the financial agents to ensure that these recipients receive reasonable access to their funds.[1] In this way, the traditional relationships between Treasury and its Financial Agents and between depositories and their depositors can be maintained.

Accordingly, we believe that the regulations should address three topics: 1) the relationship among Treasury, the Financial Agent and Direct Federal benefit recipients, 2) guidelines for EBT accounts for the receipt of direct federal benefits, and 3) qualification as a financial agent for the disbursement of direct federal benefits. We agree that it remains necessary that regulated financial institutions continue to be charged with the disbursement of direct federal benefits. For those persons who have not chosen a financial service provider for the electronic distribution of direct federal benefits, Treasury can require that the Financial Agent offer such account services to recipients as a condition of serving as a Financial Agent, because such services are a reasonable duty in connection with the obligation to disburse such funds.

We believe that those stipulated deposit account services should include the following:

- deposit accounts must be eligible for federal deposit insurance.

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[1] Treasury may also wish to request alternative methods of delivery of Direct Federal Payments, such as through the use of stored value or Smart Cards, which may offer different degrees of consumer protection. Given the recent development of this technology, these alternative methods may have more appeal to certain consumers than traditional deposit accounts.

- deposit account services must comply with all applicable laws and regulations concerning the maintenance of consumer accounts, including compliance with Regs D, E and CC.

- Because these accounts are necessary for compliance with the DCIA, there should be restrictions on the Financial Agent's ability to terminate the account relationship; however, the Financial Agent should be permitted to use another payment mechanism in cases of fraud or abuse.

- There should be guidelines for access to the account through the use of Automated Teller Machines and POS terminals; however, the use of the Benefit Security Card mark should not be mandatory. We do not see any purpose served in requiring use of the mark. Among the private rules that have developed in the EFT world are the Quest Rules required by a number of States for their EBT projects. Moreover, because of the extensive branding of ATM and POS networks, we believe that the Benefit Security Card mark would use valuable space on the back of the card and offer no commercial benefit for accessibility. We believe that FMS should join the States and accept the Quest mark and its rules for use with Direct Federal EBT.

- As to the terms and conditions for a deposit account, we believe that the consumer interest is best served by using the Treasury's Invitation for Expression of Interest process. Use of the IEI is Treasury's surest mechanism to obtain a field of bidders qualified to provide the stipulated account services. It is also an excellent method to determine the additional services or benefits that potential Financial Agents might be willing to offer as either terms and conditions for a deposit account or other methods of distribution of benefits such as through use of Smart Cards and other stored value mechanisms. This competition should serve to enable Treasury to offer the best commercially available terms for deposit accounts having the attributes desired by Treasury, as well as offering these recipients alternatives to deposit accounts.

With these minimums, Treasury will provide unbanked recipients both the financial services and consumer protections that are available to banked recipients and ensure a safe, reliable and economical means for unbanked recipients to access their benefits and treat them in the same manner as other recipients of direct federal benefits.

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Citibank EBT Services appreciates this opportunity to comment on the proposed regulation and the issues raised in connection therewith. If FMS has questions concerning this letter or would like Citicorp to provide further information, please do not hesitate to contact me at (773)380-5712.

Regards,

Loren Karnick
Senior Counsel
Citibank EBT Services
